

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF WILLOW CREEK SEWER)	
SYSTEM FOR A RATE ADJUSTMENT)	CASE NO. 97-459
PURSUANT TO THE ALTERNATIVE RATE)	
FILING PROCEDURE FOR SMALL UTILITIES)	

ORDER

On December 10, 1997, Willow Creek Sewer System ("Willow Creek") applied for Commission approval of a proposed increase in its rates for sewer service. Willow Creek determined its pro forma revenue requirement to be \$102,856, an increase of \$52,664 over its normalized revenues of \$50,192.

Willow Creek Homeowner's Association, Inc. ("Homeowner's Association"), by counsel, filed a motion to intervene. Robert L. Madison, a homeowner and customer acting on his own behalf, also moved to intervene. Both motions were granted.

In April 1998, Commission Staff began a limited review of Willow Creek's financial records and issued a Staff Report on June 24, 1998. The report recommended a revenue requirement of \$74,820 or a \$22,823 increase over Staff's normalized revenues of \$51,997.

By Order dated June 24, 1998, all parties were advised to file comments on the Staff Report or to request a hearing or informal conference within 10 days of the date of the Order or the case would stand submitted to the Commission for decision. On June 30, 1998, the Homeowner's Association filed a motion for an informal conference. By letter dated July 1, 1998, Willow Creek also requested an informal conference.

At the informal conference held on July 22, 1998, the Homeowner's Association presented information about reported service problems and questioned whether customers will receive better service if rates are increased. The Homeowner's Association was advised that case law prohibits the Commission from tying rates to quality of service; however, a formal complaint regarding quality of service may be filed pursuant to 807 KAR 5:001, Section 12.

At the informal conference, Willow Creek pointed out it had made many improvements since acquiring the system in 1981. The utility also stated its disagreement with several aspects of the Staff Report and expressed the intention to file additional supporting evidence. On August 10, 1998, Willow Creek filed written arguments with the Commission expressing disagreement with Staff's reduction of the owner-manager fee, reduction of the routine maintenance fee, disallowance of the monthly fee paid to Martin & Associates, and disallowance of interest expense.

Willow Creek argued in its August 10 filing that the \$3,600 owner-manager fee allowed in the Staff Report and the projected profit combined are not adequate compensation for the duties involved in operating a sewer utility or for the inherent liabilities of owning a sewer system. The utility stated that comparison of an owner-manager to a water district commissioner is not appropriate since there are usually three water commissioners, they have no hands-on day-to-day duties, and are not liable for any losses due to operational problems. Willow Creek contends that the background of its owner as a registered professional engineer with 45 years experience justifies a higher fee.

Willow Creek's August 10 filing requested a monthly routine maintenance fee of \$875. The proposed contract included with the filing increased the number of plant visits to two per weekday plus one week-end check and required a weekly check of the plant by a supervisor. The filing also included bids to operate the plant from Eubank, Hall and Associates, Inc. and F & W Operations for \$925 and \$965 per month, respectively.

Willow Creek's filing stated that the services provided by Martin & Associates are necessary and include recordkeeping, correspondence, and representation at meetings with the Department of Natural Resources ("Natural Resources"). Samples of the computer spreadsheets that compile the discharge monitoring report ("DMR") results and the correspondence prepared by Martin & Associates were provided. Willow Creek contends the spreadsheets are necessary in refuting claims of improper operation made by Natural Resources.

The Staff Report disallowed interest expense because the majority of the bank note proceeds had been used for purposes other than capital expenditures. More than half of the proceeds from the note was used to pay off related party loans. During the informal conference, Willow Creek disputed Staff's disallowance by contending that the related party loans were initially required for capital expenditures. Information regarding the disposition of the bank note proceeds and expenditures for sewer operation expenses for 1996 through 1998 were included in the August 10 filing.

Staff reviewed the supporting arguments and filed a response on September 1, 1998 stating that no amendments to the Staff Report would be made as a result of Willow Creek's filing. On September 2, 1998, the Commission issued an Order that

allowed 10 days for any party of record to file a request for hearing or a position statement. If no request for hearing were received, the case would stand submitted to the Commission for decision.

The Commission, after considering the record and being otherwise sufficiently advised, finds that:

1. No additional evidence or request for hearing has been filed within the time set by the Commission.

2. Regarding the owner-manager fee, the Commission notes that Willow Creek is a relatively small utility that should require minimal attention from the owner-manager since routine maintenance, repairs, sludge hauling, billing and collection, and book-keeping are all contracted services. Although Willow Creek argues that the owner-manager fee should not be standardized since the work performed by treatment plant owners varies, there is no way to know how much time any owner-manager, including Willow Creek's, devotes to a utility since time records are typically not maintained. None of the information filed in this case compels a change in the limitation of the owner-manger fee to \$3,600.

3. In reviewing the routine maintenance fee, it was noted that the test year contract required one visit per day. There is evidence in the record that the plant experienced significant operational problems despite the contractual provisions for daily visits by the plant operator. There is no explanation of why these problems occurred with this level of oversight, and there is no evidence that twice-daily visits would significantly improve the operation of the plant.

Willow Creek requested that contract proposals for routine maintenance include a weekly inspection by a supervisor to ensure the plant is being properly operated and maintained. Any service provider for routine maintenance would be bound by contract to ensure that the plant is properly operated. If a subcontractor provides the service, the service provider would still be expected to ensure that the work is being done properly and should not receive additional compensation for verifying that the basic contract provisions are being met. Staff's limitation of routine maintenance to the test year level of service and expense is reasonable.

4. In evaluating the disallowance of the monthly fee paid to Martin & Associates, the Commission observes that the preparation of correspondence and attendance at meetings with Natural Resources are considered to be management duties and are compensated by the owner-manager fee. Willow Creek argued that the computer worksheets aid in refuting claims of improper operation; however, these appear to be compilations of DMR results and it is not clear why the original DMR documents would not serve the same purpose. Staff's disallowance of the monthly fee paid to Martin & Associates is reasonable.

5. The issue of Staff's disallowance of interest expense was considered and none of the information included in the August 10 filing supported the applicant's argument made during the informal conference that the related party loans were initially required for capital expenditures. Just over half of the related party loans were made in 1995 but there were no capital expenditures during that year according to the depreciation schedule filed with Willow Creek's initial application. The remaining related party loans were made in 1996 when the only capital expenditure was for a \$3,675

blower. However, based on the dates provided, none of the loans were actually used to purchase the blower. The information filed in the case supports the finding that the majority of the bank note proceeds were used for purposes other than capital expenditures, and that the interest should not be included in pro forma operations.

6. The recommendations and findings of the Staff Report are supported by the record, are reasonable, are adopted as the findings of the Commission in this proceeding, and are incorporated by this reference.

7. The rates in Appendix A, attached hereto and incorporated herein, are the fair, just, and reasonable rates for service provided by Willow Creek and will produce annual revenues of \$74,820. These rates will allow Willow Creek sufficient revenues to meet its operating expenses and provide for future equity growth.

8. The rates proposed by Willow Creek will produce revenue increases that are unreasonable and thus inconsistent with KRS 278.030.


IT IS THEREFORE ORDERED that:

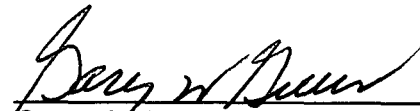
1. The rates proposed by Willow Creek in its application are hereby denied.
2. The rates contained in Appendix A are approved for service rendered by Willow Creek on and after the date of this Order.
3. Within 30 days of the date of this Order, Willow Creek shall file with the Commission its revised tariff setting out the rates approved herein.

Done at Frankfort, Kentucky, this 9th day of October, 1998.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 97-459 DATED OCTOBER 9, 1998

The following rates and charges are prescribed for the customers in the area served by Willow Creek Sewer System. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

Sewer Rates

Single Family Residential

\$18.45 per Month